Real Estate Investment Trust in India: Opportunities and Challenges ahead

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Abstract

An undeveloped capital and debt market, combined with constrained alternatives for bringing reserves has come about up in critical blockage of money for engineers who own business resources. In any case, the segment which saw impressive headwinds after the Global Financial Crisis of 2009, has noticed some indication of recuperation in the last couple of years. Since most recent two years private value firms have demonstrated more enthusiasm for getting business resources on the back of diminishing opening, fairly adjustment of rentals and devaluation in the Indian money. These organizations have exploited the liquidity circumstance and have gained resources at appealing cost. Still, a huge extent of prepared business resources are still possessed by designers who keep on evaluating roads to offload these benefits. The dispatch of REITs in the present times is required to be significant alleviation for engineers and could be an imperative change, brought into the land part, as of late.

Introduction

The liberal and to some degree adaptable monetary approaches received by the Indian government to enhance private interest have helped in reinforcing the nuts and bolts of the Indian economy which incorporates the youthful populace, fast developing urbanizations and mounting middleclass populace. The GDP of the nation has quadrupled since the year 2000 to achieve USD1.8 trillion in 2012 and is relied upon to end up the third biggest economy worth USD 6.6 Trillion by 2028. The land division in India has been a fundamental recipient of the solid and consistent monetary development saw in India since the year 2000. The improvement in the area, which has been bolstered by arrangement of changes, has not just brought about huge private and business land, additionally has supplemented the development of physical and social base of the nation also.

The land part has improved the interest for more than 250 auxiliary businesses, which incorporates steel, concrete, paint, and development material, and the center is at the development business. This area is one of the key drivers of the Indian economy as it is considered as the second biggest generator of business open doors beside agribusiness. Land Investment Trusts (REITs) were reported in the Union Budget 2014–15 to encourage financial specialists to all things considered put resources into business properties and win benefit. The draft meeting paper on Real Estate Investment Trust (REIT) Regulations, 2013 was reported by Securities and Exchange Board of India (SEBI) on October 10, 2013. In 2008, SEBI had issued certain draft controls for presenting REITs. REITs in India would issue securities, that will be recorded on the stock trades and REITs will put resources into finished rent creating properties in India and home loan supported securities. Initially I-REITs should be accessible and open just to high total assets people and organizations. In the end, it is opened to retail financial specialists too. The demographic flow of Indian populace are evolving quick, prompting a perpetually developing interest for quality land that keeps on being higher than supply. REITs can bring the required ventures for taking care of this expanding demand.

Objectives of the study

1. To conceptually understand REIT and the various types of REIT which are existing today.
2. To understand and identify the significant reasons for introducing REIT in India.
3. To understand the REIT regulations in India.

Real Estate Investment Trust-A theoretical framework

REITs are speculation trusts which are like common assets with the main significant distinction being that as opposed to utilizing the cash which is gathered from financial specialists we purchase stocks and bonds. It resembles a pooling framework through which capital is conveyed to possess land resources. REITs give financial specialists of various types with plans of normal salaries, broadening and capital thankfulness in the long haul. REITs pay out the greater part of their assessable wage as profits to the shareholders. The shareholders consequently, should pay the assessments on the profits got. REITs permit interests in the arrangement of vast scale and huge properties as the venture is made in different enterprises by obtaining the stock. Essentially shareholders are profited by owning stocks in different organizations, the holders of a REIT can gain an offer of the salary made through land venture – without really going out and purchase or back the property.

In today's situation, REITs exists in all parts of the economy, including flats, doctor's facilities, inns, mechanical offices, foundation, nursing homes, workplaces, shopping centers, and so forth. At the worldwide level there are three sorts of REITS. In India notwithstanding, a starting has been made with the third sort that is the hybrid one.

Equity REITs: Such sort of REITs has and works pay delivering land and performs renting, improvement, and development exercises. Equity REITs bit by bit have turned out to be land working organizations that take part in an extensive variety of land exercises, including renting, improvement of genuine property and occupant administrations. The real distinction amongst REITs and other land organizations is that a REIT must get and build up its properties fundamentally to work them as its very own component portfolio rather exchange them once they are created.

Mortgage REITs: Such kind of REITs loans cash straightforwardly to land proprietors and administrators or develops credit in a roundabout way through the obtaining of advances or home loan sponsored securities. Mortgage REITs by and large augment contract credit just on existing properties. A few home loan REITs additionally deal with their financing cost hazard utilizing securitized contract ventures and element supporting strategies.

Hybrid REITs: Hybrid REITs is a consortium of both the speculation systems of owning properties and making advances.

Sector-Specific Types of REITs

Housing REITs – Such REITs buy, patch up, lease and oversee lodging properties situated in the business sectors to produce rental pay. They hold properties over the long haul and produce for all intents and purposes all income by renting the properties. The salary produced is utilized to pay for operational expenses and is appropriated as profits among shareholders.

Industrial REITs – Industrial REITs obtain, own and oversee modern properties, for example, stockrooms, structures, undeveloped area, business parks and cutting edge space. The occupants of modern REIT properties are boundless and cut crosswise over different sorts of business exercises.

Hotel REITs – These REITs own inn, cabin or resort properties furthermore incorporate distinctive sorts of properties, for example, restricted administration, resorts, gatherings focus, suite and air terminal properties. Inn REITs get cost from the hidden estimation of lodging properties the REIT claims and from the wage produced by those properties.

There likewise exists private, non-recorded and open REITs. Majority share of the REITs are managed on the most perceived stock trades. Singular speculators are permitted to put resources into REITs either by buying their shares specifically on an open trade or by putting resources into a common reserve that has practical experience in broad daylight land part. An additional benefit in putting resources into REITs is the way that numerous are joined by profit reinvestment arranges (DRIPs). The most extreme advantage will be that of speedy and simple liquidation of interests in the land market not at all like the conventional method for discarding land.

Structure of REITs

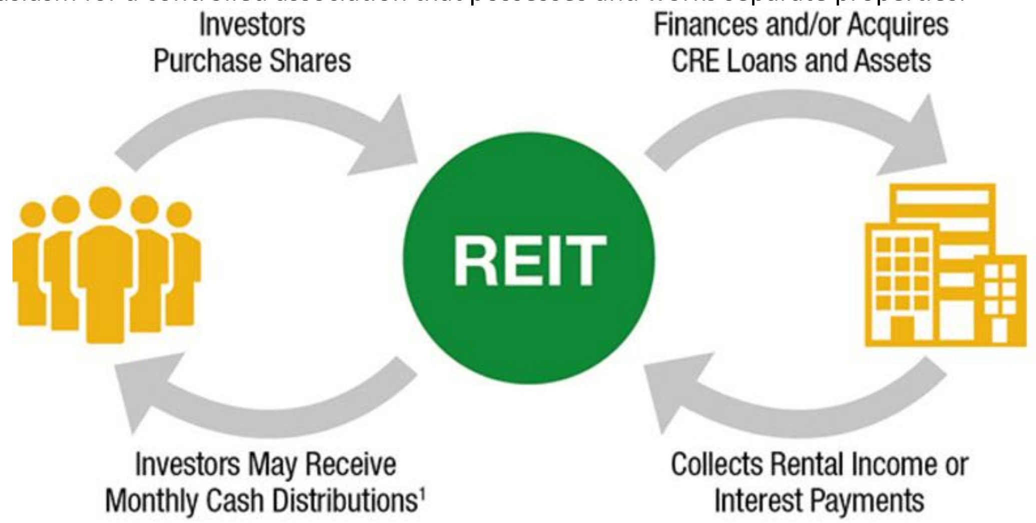
REITs are regularly organized in one of three ways:

- Traditional,
- UPREIT and
- DownREIT

A customary REIT is one that possesses its advantages straightforwardly rather than a working association. In the UPREIT, the accomplices of an Existing Partnership and REIT get to be accomplices in another association named the Operating Partnership. For their separate advantages in the Operating Partnership ("Units"), the accomplices contribute the properties from the Existing Partnership and the REIT contributes the money.

After a timeframe (frequently one year), the accomplices may appreciate the same liquidity of the REIT shareholders by offering their Units for either money or REIT offers (at the choice of the REIT or Operating Partnership). Such change may bring about the accomplices causing the duty conceded at the UPREIT's arrangement. The Unit holders may delicate their Units over a timeframe, in this way spreading out such assessment. What's more, when an accomplice holds the Units until death, the domain charge rules work so as to give that the recipients may delicate the Units for money or REIT offers without paying pay charges.

A DownREIT is organized much like an UPREIT, however the REIT claims and works properties other than its enthusiasm for a controlled association that possesses and works separate properties.



Significant Reasons for Introducing REITs in India

1. ***Rise sought after because of changing demographics and increment in urbanization***: according to the assessments of UN, India has the most astounding rate of progress of urban populace among the BRIC countries. It is anticipated that 843 million individuals will dwell in Indian urban areas by the year 2050, which is the same in the event that we consolidate the number of inhabitants in the Japan, Brazil, Russia, US and Germany. More than 300 million people are relied upon to be added to India's working age populace by the year 2050. This would add to

developing urbanization and the requirement for giving lodging/convenience offices for this segment, which incorporates the expanding number of ladies in the work power too.

2. ***REITs will bring transparency*** – REITs will help to streamline the land division by making a straightforward instrument for bringing account up in the land market. REITs must be enlisted with SEBI which would have strict control and checking.

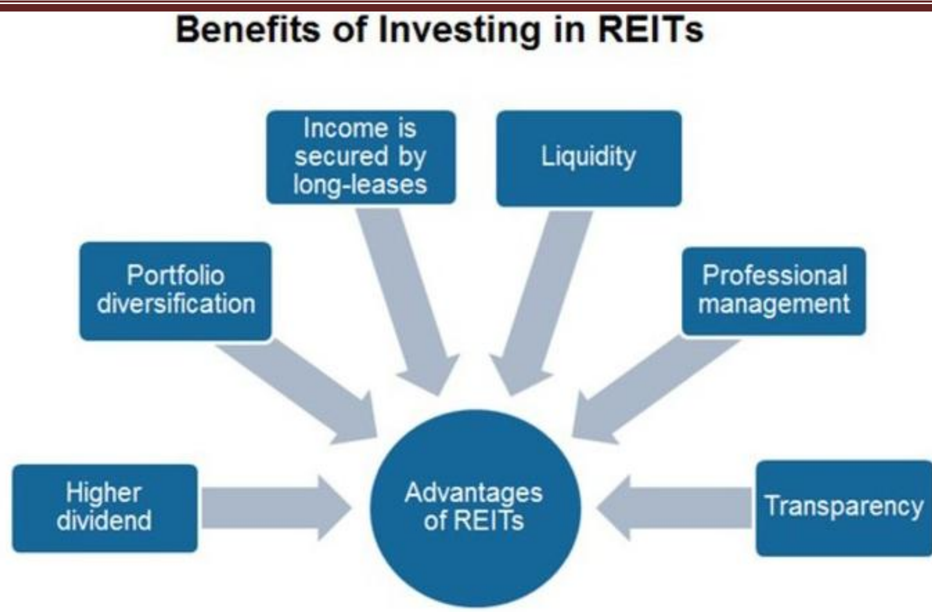
3. ***Improvement paying off debtors value extent*** – There will be a change in the obligation value extent in the land market with the presentation of REITs as it is the wellspring of the unadulterated value capital. This will get the development in more steady and develop land market.

4. ***Medium for tending to non-performing resources (NPAs)*** – REITs can be utilized as a medium to wipe out NPAs/wiped out or old organizations holding huge estimations of land generally as area. Transfer of such NPAs/organizations to REIT's will have a double impact—acknowledgment of genuine quality for the land and simplicity in selling the tired organization after evacuation of the high estimation of land from its books.

5. ***New parkway for speculation*** – REITs are reasonable for those speculators who wish to differentiate their benefits past gold and value markets. REITs would be capable anticipated that would give a sheltered and expanded venture alternative at the lower hazard, all under expert administration, which guarantees the most noteworthy profit for the speculation. A speculator can procure two sorts of salary from REITs. One is through the capital increases when the units of REITs are sold on stock trades and the other is through profit pay.

REITs an attractive investment

Firstly, REITs creates income in type of rental-wage. We realize that rental pay from land is exceptionally guaranteed. This conviction of wage era makes REITs a moment hit with financial specialists. Also, one can purchase REITs from solace of home with snap of a catch; though purchasing a physical-property is over 30 days exercise. On a normal REITs can yield near 10% for each annum returns for its shareholders.



India REIT Regulations -A Holistic Perspective

The Securities and Exchange Board of India (SEBI) notified the SEBI (Real Estate Investment Trusts) Regulations, 2014 and SEBI (Infrastructure Investment Trusts) Regulations 2014 on 26th September 2014 and laid down a framework for Real Estate Investment Trusts (REITs) and Infrastructure Investment Trusts (InvITs) and their registration and regulation in India. As per these regulations, both REITs and InvITs have to be registered as Trusts under the Indian Trusts Act, 1882. SEBI had introduced legal framework for real estate mutual funds on 16th April 2008 by way of SEBI (Mutual Funds) (Amendment) Regulations, 2008 and inserted Chapter VI A – Real Estate Mutual Funds Schemes (REMFs) and that for Infrastructure Debt Funds was added by inserting Chapter VI B - Infrastructure Debt Fund Schemes on 30th August 2011 to the Securities and Exchange Board of India (Mutual Funds) Regulations, 1996.

The SEBI (REITs) Regulation 2014:

Particulars	**Regulations**
Sponsor	• Maximum number of sponsor restricted to 3 • Minimum holding for each of the sponsor shall be equivalent to 5% of the no. of units of REITs (i.e. Post initial offer size) • Aggregate Net worth of sponsors shall be of atleast Rs 100 crores. Moreover minimum networth requirement for individual sponsor is Rs 20 crores. • Minimum 5 years experience in development of real estate or fund management in real estate industry. Moreover, where the sponsor is a developer, at least two projects have been completed.
Manager	• Minimum Net worth Rs. 10 Crores. • Minimum 5 years experience in fund management or advisory or property management in the real estate industry. • Atleast 50% of directors or members of governing body as

	independent and not directors or members of governing body of another REITs. • Entered into an investment management agreement with the trustee which provides for the responsibilities of the manager in accordance with regulation 10
Trustee	• Registered with SEBI under SEBI (Debenture Trustees) • Regulations, 1993 and not an associate of the sponsor or manager. • Having such infrastructure and personnel as specified by SEBI.
Minimum Asset Criteria for listing	• In order to offer units to public the value of all the assets owned • by REIT should be at least Rs 500 crores. • The offer size is not less than Rs. 250 Crores. • Initial offer of REIT units has to be through public issue only.
Investment Conditions	• Investments only permitted in following channels: ○ SPVs (only if SPV holds 80% of the properties directly) ○ Properties ○ Securities ○ TDRs (Transferable Development Rights) • Can't invest in vacant land, agriculture land and mortgages other than mortgage backed securities. • At least 80% of the value of REIT shall be invested in completed and rent generating properties. Lock-in-period of 3 years from date of purchase. • Investment in TDRs and Unutilized Floor Space Index (FSI) now permitted under second tier of Investment mode with a maximum cap of 20% of REIT's Assets. • If investment in under construction properties under the sub second tier of Investment mode with maximum cap of 10% of REIT's Assets then, lock-in-period of 3 years from date of completion. • Not less than 75% of the revenues of REITs and SPVs, other than gain arising from disposal of properties, shall be from rental, leasing and income incidental to leasing of real estate.
Approval of Unit-holders	• In case of sale of properties of REIT or SPV exceeding 10% of the value of assets. • Purchase of property for a value greater than 110% of the value as assessed by valuer or sale of property which is less than 90% of the value as assessed by the valuer is allowed if approved by Unit Holders (Valuation by two independent valuers is mandatory). • In case of transactions with related parties on crossing of stipulated norms. • If the aggregate consolidated borrowings and deferred payments of the REIT net of cash and cash equivalents

	exceed twenty five per cent. of the value of the REIT assets, credit rating from credit rating agency is also required along with approval of unit-holders. • With respect to the annual meeting of unit holders, approval of ○ latest annual accounts and performance of the REIT ○ auditor and fees of such auditor, as may be required ○ latest valuation reports ○ appointment of valuer, as may be required ○ any other issue including special issues as specified ○ under subregulation (6) • Any issue, in the ordinary course of business, which in the opinion of the sponsor(s) or trustee or manager, is material and requires approval of the unit holders. For instance- Any change in manager including removal of the manager or change in control of the manager, any material change in investment strategy or any change in the management fees of the REIT
Cash Flows	Not less than ninety per cent of Net distributable cash flows of the REIT shall be distributed to the unit holders once in 6 months. • However if sale proceeds from any property are reinvested in another property then there is no requirement of distributing 90% of the proceeds to the Unit Holders.
Related Party Transactions	• Transactions such as acquisition or sale of properties or investments into securities in a financial year; or • Value of funds borrowed from related parties in a financial year requires previous approval of Unit holders if the value of transaction exceeds 10% of the value of REITs or consolidated borrowings respectively
Borrowings	• Aggregated consolidated borrowing and deferred payment of REIT net of cash and cash equivalents shall never exceed 49% of the value of REIT assets.
Valuations	• The valuer shall not be an associate of the sponsor(s) or manager or trustee and shall have not less than five years of experience in valuation of real estate. • Full valuation report shall include the mandatory minimum disclosures as specified in Schedule V to these regulations. • A full valuation shall be conducted at the end of financial year i.e at 31st March by the valuer within 3 months along with half yearly valuations. • Prior to any issue of units to the public and any other issue of units as may be specified by the Board, the valuer shall undertake full valuation of all the REIT assets and include a summary of the report in the offer document.

The International Presence of REIT

More than 30 countries around the world have established REIT regimes. The spread of the REIT approach to real estate investment around the world has also increased awareness and acceptance of investing in global real estate securities.

Singapore REITs:

Some of the regulations that S-REITs have to adhere to includes:

- Maximum gearing ratio of 35%
- Annual valuation of its properties
- Restriction to certain types of investments the S-REITs can make
- Distribution of at least 90% of its taxable income

Currently there are 5 REITs listed on Singapore Stock exchange. They represent a range of property sectors including retail, office, industrial, hospitality and residential.

USA REITs

USA is the birthplace of REIT IN 1960. Some of the regulations that USA-REITs have to adhere to includes:

- Taxed in such a way that they usually distribute all their income.
- Must be owned by at least 100 people, no more than 50% of equity
- Must derive at least 75 percent of gross income from rents from real estate or interest on mortgages on property
- Must invest at least 75 percent of its total assets in real estate assets

Challenges Ahead

The Indian REIT regime is at par with the international REIT format and seems to have what is needed to provide the right impetus to the Indian real estate sector. In India, in the absence of a regulator for the real estate sector, introduction of REITs is a good move that will help bring in liquidity, transparency, better governance, organized platform for retail investment, an ecosystem, which is professionally managed and protects investors.

The real estate industry is at the centre of construction industry which in turn encourages the demand for more than 250 ancillary industries, including steel, cement, paint, and construction material. It also provides the huge employment opportunities and it is considered as the key drivers of the Indian economy. But, this industry has faced many ups and downs in the last few years such as increase in input costs, rising financing costs, inadequate funds, etc., are some of the serious concerns that are impeding the performance of the Indian real estate industry. REITs will offer another opportunity to the investors. It will offer dividend which is comparatively higher than other investments. Thus, the investor can earn high annual dividends as well as there will be capital appreciation in the value of the properties.

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